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RHEHNSC/NATIONAL SECURITY COUNCIL WASHINGTON DC PRIORITY
RHMFISS/DEPT OF ENERGY WASHINGTON DC PRIORITY
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S E C R E T SECTION 01 OF 02 VILNIUS 000618

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DEPT FOR U/S SHINER, EUR/FRIED AND EB/WAYNE/SULLIVAN
DOE FOR HARBERT
DOC FOR 4231/IEP/EUR/BOHIGIAN
NSC FOR GRAHAM, MCKIBBEN AND COEN
TREASURY FOR LOWERY, LEE AND COX

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TAGS: [PREL](#) [EPET](#) [ECON](#) [LH](#) [RU](#) [VE](#)
SUBJECT: TWO RUSSIAN OIL SUPPLIERS CANCEL JULY CRUDE
SHIPMENTS TO LITHUANIAN REFINERY

REF: A. VILNIUS 609
[1](#)B. VILNIUS 512 AND PREVIOUS
[1](#)C. VILNIUS 285
[1](#)D. WARSAW 1336
[1](#)E. KELLY-PEKALA 01 JUL 06 E-MAIL

Classified By: Economic Officer Scott Woodard for reasons 1.4 b and d

[1](#)1. (C) SUMMARY: RosNeft and Vitol have cancelled their crude shipments to Lithuania's Mazeikiu Nafta oil refinery (MN) for July, leaving the refinery with only half of the crude it expected to process this month. The shortfall will affect Latvia and Estonia as well as Lithuania. MN, which currently brings in all of its crude via pipeline from Russia, has the technical capability to use its Baltic Sea terminal to offload crude from tankers and transport it by pipeline to the refinery. Arranging the supply and transportation contracts for this change, according to MN's general manager, would probably take at least a month, and the refinery only maintains stocks sufficient for about six days of operations. GOL officials will consult with PKN Orlen this week to discuss the situation. END SUMMARY.

SOME RUSSIAN SUPPLIERS CUT CRUDE SHIPMENTS

[1](#)2. (C) MN General Manager Nelson English (protect) told us on June 30 that Vitol had abruptly and inexplicably cancelled its contract June 29 to supply 200,000 tons of crude to MN in July. English, an Amcit who has always shared the latest MN information with this Mission, told us on July 3 that RosNeft cancelled its July contract on June 30 to supply 200,000 tons of crude. This, English explained, left MN with only half of the crude supply it expected for July: 409,000 tons. (English explained that the vast majority of MN's supply agreements are spot or spot-like contracts that do not have penalty clauses for non-performance, which gives suppliers the ability to break the contracts relatively cost-free.) English said that Transneft told him that it might be able to find an additional 200,000 tons for MN.

[1](#)3. (C) This turn of events was a surprise for English. As of June 28, he said, MN was completely booked for July; it had contracts to process 800,000 tons of crude during a month with traditionally high margins. During our June 30

conversation, he said that MN already had contracts for the third quarter amounting to 90 percent of the refinery's capacity. He said that MN's main suppliers were Lukoil, Vitol, TNK-BP, and RosNeft.

MANAGING A CUT-OFF

14. (C) English told us on June 30 that using the Butinge terminal to bring crude to MN posed no technical challenges. He said that it would take a maximum of 24 hours to make the engineering changes necessary to reverse the flow and pump oil from tankers to the refinery. The difficult part, he said, would involve the commercial arrangements, including negotiating new supply and transportation contracts. He explained that these arrangements would take a month or more to finalize. He emphasized that reaching agreements with suppliers would be especially difficult and costly in a situation where Russia had cut off supply, because suppliers will know that MN is in a tough situation and will therefore drive a harder (i.e., more expensive for MN) bargain.

15. (C) English said that his most immediate concern in a cut-off situation would be securing supply for the Baltic market. Forty percent of MN's production stays in the Baltics, he said, and MN only maintains an inventory of crude that would allow it to keep refining for about six days. He added that there is probably not enough supply (of crude and refined product) in the local market at present to supply the Baltic market for a month. Company officials told us in May that MN supplies approximately 95 percent of the Lithuanian market and 70 percent of the Latvian and Estonian markets.

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INTERPRETING LUKOIL'S RECENT COMMENTS

16. (C) Asked to comment on Lukoil VP Leonid Fedun's June 28 statement that Lukoil planned to cease shipping crude to Lithuania (ref A), English said that he thought that Lukoil was irritated that MN had increased the number of (Russian) suppliers it contracted with, reducing Lukoil's importance as a supplier. English told us that Lukoil supplied about 26 percent of MN's crude in 2005, but that this figure had dropped to 14 percent at present. Fedun's statement was especially surprising, English said, because Lukoil had recently told MN that it would like to double the amount of crude it supplies to the Lithuanian refinery.

STILL WORKING ON NEW SOURCES OF SUPPLY

17. (C) English told us that he would be traveling soon to Venezuela to continue negotiating with PDVSA as a possible crude supplier (ref c). The Venezuelans, he said, were "not much easier to work with than the Russians."

GOL REP WILL VISIT WARSAW

18. (C) Saulius Specius, adviser to the Prime Minister and one of the GOL's main negotiators on the sale of MN to PKN Orlen, told us on July 3 that he was rushing to Warsaw later that day to consult with PKN Orlen officials. We will contact him for a readout when he returns to Vilnius later this week.

COMMENT

19. (S) The worst-case scenario for Lithuania -- a complete

cutoff of Russian oil starting July 1 -- did not occur, but the canceling of half of the refinery's July supply contracts does not bode well for MN or for the energy security of the three Baltic republics. Neither MN nor we know why RosNeft and Vitol canceled their contracts, but the timing, soon after Fedun's statements and the information received by the GOL (ref a), is striking, to say the least. So too is the fact that Lukoil, despite Fedun's comments, has not canceled its July contract. Perhaps that shoe is yet to drop.

KELLY